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IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

168

CHICAGO & EASTERN ILLINOIS RAILROAD CO., an Indiana corporation, et al.,

Petitioners,

vs.

PAUL J. KERN and IRVING M. LESCH,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO APPELLATE COURT OF ILLINOIS, FIRST DISTRICT

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Petitioners, Chicago & Eastern Illinois Railroad Co., an Indiana corporation, Alfred MacArthur, David O. Mathews, and F. S. Yantis, pray that a writ of certiorari issue to review a judgment of the Appellate Court of Illinois for the First District. The judgment affirmed a trial court's declaratory decree that the petitioner railroad is required to have 13 directors elected for non-staggered terms unless changed by a vote of the holders of ⅔ of the railroad's Class A stock (App. C, *infra*, p. 17a, 18a).

Citations To Opinions Below.

The case was heard twice by the Appellate Court. The first opinion, reported at 31 Ill. App. 2d 300, 175 N.E. 2d

408 (1961), is reprinted in Appendix A, p. 1a. The second opinion, reported at 44 Ill. App. 2d 468, 195 N.E. 2d 197 (1963), is reprinted in Appendix D, p. 19a. An opinion of the trial court, which is not reported, is printed in Appendix B, p. 14a.

Jurisdiction.

The first judgment of the Appellate Court was entered March 1, 1961 and modified June 28, 1961 (A. 63,* App. 1a). Its second and final judgment was entered November 27, 1963 (R. 11**). A timely petition for leave to appeal to the Supreme Court of Illinois was denied March 16, 1964 (App. E, p. 31a, *infra*).

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. §1257(3). Petitioners contend that full faith and credit have been denied by Illinois state courts to Indiana statutes and that the Illinois courts have given an unlawful effect to and violated a reorganization plan under section 77 of the Bankruptcy Act. Both contentions were made in petitioners' pleading in the trial court (A. 60-2).

Questions Presented.

1. Did the Illinois courts, applying an Illinois rule of constitutional law, correctly hold that staggered terms for directors of an Indiana corporation, permitted by Indiana statute, are forbidden by a requirement of cumulative voting in a federal reorganization plan and an Indiana certificate of incorporation?

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* The references to "A," are to the printed Abstract of Record incorporated at p. 21 in the certified record from the Illinois Appellate Court.

** The reference to "R." is to the page of the certified record from the Illinois Appellate Court.

2. **Are Illinois courts forbidden by the Full Faith and Credit Clause of the United States Constitution to require an Indiana corporation to have 13 directors with non-staggered terms unless permitted by a vote of ⅔ of the company's Class A stock when Indiana statutes permit staggered terms by a vote of the directors and permit less than 13 directors by a majority vote of the stockholders?**

Constitutions and Statutes Involved.

The Full Faith and Credit Clause of the United States Constitution and a section of the Constitution of the State of Illinois are printed at Appendix G, p. 50a.

Statutes of the State of Indiana, Burns Annotated Indiana Statutes (1951 volume and 1963 supplement), secs. 55-206, 55-207, 55-208, 55-2209, and 55-2210, are printed in Appendix H, pp. 51a-55a.

Section 77(f) of the Bankruptcy Act, 11 U.S.C. 205(f) [1934 ed., Supp. V 1939], is printed in Appendix I, pp. 56a-58a.

STATEMENT OF THE CASE.

The petitioner railroad was incorporated in Indiana in 1940 (A. 117-8) pursuant to a reorganization plan and decree (A. 2, 58-9) which reorganized a former Illinois corporation under Section 77 of the federal Bankruptcy Act (11 U.S.C. 205). The plan, which had been approved by the Interstate Commerce Commission, *C. and E. I. Ry. Co. Reorganization*, 230 I.C.C. Rep. 571 (1939) and Appendix F, p. 33a, provided for the transfer of the debtor's property to a new corporation to put the plan into effect (App. 34a). The plan directed that the two classes of corporate stock should have the right of cumulative voting in electing directors and that the company should have

a board of directors of 13 members with terms of one year (App. 44a, 45a, 48a).

An Indiana statute concerning the formation of railroad corporations was amended February 23, 1939 to provide for the incorporation of any railroad organized under section 77 of the Bankruptcy Act (App. 53a). The United States District Court for the Northern District of Illinois approved the plan in June 1939 (A. 50). In June 1940 the District Court found that a proposed certificate of incorporation and proposed bylaws for a new Indiana corporation conformed to the reorganization plan (A. 51-2).

The certificate of incorporation of the Secretary of State of Indiana was dated June 27, 1940 (A. 152-3). The certificate directed the immediate issuance of 383,862½ shares of Class A stock and 343,297 shares of common stock (A. 135). All stockholders were given the right of cumulative voting ("to cast as many votes as shall equal the number of his shares multiplied by the number of directors to be elected, and to cast all of his votes for one candidate or to distribute his votes among the candidates, as he shall see fit"); and the consent of ⅔ of the holders of Class A stock was required for certain amendments to the certificate or bylaws (A. 143). The certificate stated that the number of directors should be 13 (A. 145). Amendment of the certificate was provided for "in the manner prescribed by statute" (A. 150). The corporate bylaws stated that each director should hold office until the next annual meeting of the stockholders and that the bylaws could be amended by the directors (A. 53, 173).

The general railroad statute of Indiana governing petitioner railroad provided that directors should hold office for one year and until others are elected in their places

(sec. 55-206, App. 52a); that the stockholders at an annual meeting could determine that the directors should consist of any number not less than five nor more than 13 (sec. 55-207, App. 52a); and that the directors could classify the members of the board so that the terms of ¼ of the members would terminate at the first annual election after classification and ¼ at each election thereafter (sec. 208, App. 53a).

In July 1953 the directors amended the bylaws to provide staggered terms for the directors (A. 31-2). At meetings in 1954, 1955, 1956, 1957, and 1958 the stockholders voted for directors for staggered terms as provided in the 1953 bylaw (A. 5-6, 31). Respondent Paul J. Kern so voted his shares and others by proxy in the years 1955 through 1958 (A. 12-3, 31-9). During these years Mr. Kern and the railroad's president had conversations which are described in conflicting affidavits (A. 41, 65). During March through October 1958 Mr. Kern corresponded with the railroad's president and secretary concerning the 1953 bylaw (A. 23-31, 43-7). On October 29, 1958 Mr. Kern made formal demand for its repeal (A. 25-6). The board of directors repealed the bylaw at its next meeting held November 14, 1958 without knowing that the present suit had been filed on November 12, 1958 (A. 3, 14, 24-5).

Respondent Kern, owning 4,000 shares of Class A stock, sued on behalf of all owners of Class A stock (A. 3, 7). At that time approximately 75,000 shares of Class A stock and 426,000 shares of common stock were outstanding (A. 5). The staggered terms of directors under the 1953 bylaw were alleged to violate the plan of reorganization, the decree of the United States District Court, and the certificate of incorporation (A. 6). On March 8, 1960 the trial court dismissed the suit on petitioners' (defendants') motion (A. 56).

Respondents appealed to the Appellate Court, which reversed and remanded (Opinion, App. 1a). The court rejected the defense that the case was moot by reason of the repeal of the 1953 bylaw on November 14, 1958 (App. 3a-4a). The opinion said that the suit seeks "a declaration of the rights of stockholders", that the directors could revert to staggered terms at any time and prejudice the Class A stockholders ability to elect directors by cumulative voting. The case was held to be excepted from the mootness doctrine by "the substantial public interest involved" because the railroad is a "large public service corporation" with its stock listed on the New York Stock Exchange and widely held; and there is a "wide general interest in the stability of preferred stock" (App. 4a). Estoppel and other defenses were also rejected (App. 9a-11-a).

The 1939 reorganization plan and the certificate of incorporation were held to forbid staggered terms. The principal issue was said to be whether the 1953 amendment violated

> "a provision for cumulative voting and annual election of all directors, as contained in a reorganization plan, a decree of court and the articles of incorporation" (App. 1a).

The opinion noted that the reorganization plan

> "included a provision for the issuance of Class A preferred stock with the right of cumulative voting in the election of directors and for a board of thirteen members, each director to serve one year". (App. 1a).

The basic legal question was said to be whether the power of minority shareholders to cumulate votes "should be diminished or extinguished" in contravention of the reorganization plan and certificate of incorporation. For,

the opinion said, citing *Wolfson* v. *Avery*, 6 Ill. 2d 78, 81-82, "that is the natural end result of classified directorships and staggered elections" (App. 4a).

The necessity of enforcing the reorganization plan was emphasized (App. 6a-7a):

> "When a reorganization plan has been certified by the Interstate Commerce Commission and approved by the court, as has been done in this case, that plan becomes final, is binding upon the debtor and all other interested parties, and must be enforced as written. 11 U.S.C.A., secs. 205, 624; *Denver & R. G. W. R. R.* v. *Goldman Sachs & Co.*, 212 F. 2d 627 (10th Cir. 1954). The plan of reorganization unconditionally fixes the term of each director at one year. There is nothing in the language of the certificate of incorporation which negates this clear and unambiguous language embodied in the Commission order."

Answering petitioners' contention that cumulative voting was not a special right of the Class A shareholders since the common stock shareholders had the same right, the opinion again returned to the reorganization plan (A. 9a):

> "The answer to this contention is that preferred shareholders are preferred, and that the rights which protect them against dilution of their power to elect directors were given to them by the plan of reorganization and the certificate of incorporation."

And again (App. 9a):

> "The violation of their [respondents'] rights is in contravention of an Interstate Commerce Commission order, the plan of reorganization, the Federal court decree, and the certificate of incorporation. We are of the opinion that estoppel is inapplicable."

In a final paragraph on the reorganization plan, the opinion said weight had been given to it but explained (App. 11a):

". . . we felt that the plan had a strong bearing on the proper construction and interpretation of the articles of incorporation and the bylaws. We do not hold that the reorganization plan and agreement is now binding on defendant corporation. The basic document on which plaintiffs' right must be determined is the certificate of incorporation."

On remandment petitioners (defendants) filed an answer alleging (A. 57-63) that petitioner railroad was governed by its certificate of incorporation and bylaws under Indiana law; that the 1953 bylaw did not violate the certificate of incorporation but was in accord with it and Indiana statutes cited in the answer; that the relief sought would violate the Full Faith and Credit Clause of the United States Constitution; that the controversy became moot when the 1953 bylaw was repealed in 1958; and that recovery was barred by laches and estoppel (A. 62).

Respondents made motions on the pleadings and for summary judgment (A. 64-5); petitioners filed affidavits in opposition (A. 65, 66, 117). The trial court wrote an opinion and entered a summary decree in respondents' favor (App. B and C, pp. 14a-18a). The opinion stated that the Appellate Court had adjudicated that the certificate of incorporation, "construed in the light of the plan of reorganization," fixes the number of directors at 13 and provides for non-staggered one year terms of office for such directors with cumulative voting rights (App. 14a-15a). The decree declared that the railroad's certificate of incorporation "requires that said railroad have a board of thirteen directors elected for uniform terms of one year each with cumulative voting by shareholders" and that the consent of the holders of at least ⅔ of the outstanding Class A stock was necessary to amend these requirements (App. 17a-18a).

The Appellate Court affirmed in a second opinion (App. 19a); held that the case was not moot in a detailed discussion of the law, including federal cases (A. 20a-26a); stated that the court's other rulings on the first appeal were the law of the case that would not be considered again (A. 26a); and concluded that the Indiana statutes relied on by petitioners (defendants) "did not raise any questions of law or fact" (App. 28a).

The Illinois Supreme Court denied the petition for leave to appeal on March 16, 1964 (Appendix E, pp. 31a-32a).

REASONS FOR GRANTING REVIEW

The Illinois courts have wrongly decided two substantial federal questions which, so far as we are aware, have never been decided by this Court. The 1939 reorganization plan under the Bankruptcy Act and the Act itself have been misapplied by reading into the pla an irrelevant Illinois rule of substantive law and by using the plan to prevent future corporate changes. Instead of looking to Indiana statutes to determine the legal effect of an Indiana certificate of incorporation, the Illinois courts have applied an Illinois rule of substantive law in violation of the Full Faith and Credit Clause of the United States Constitution.

These errors are the sole support for the specific declaration that the railroad must have 13 directors with non-staggered terms unless the holders of ⅔ of the Class A stock consent to a change. The rulings go further in broadening the rights of cumulative voting and a ⅔ vote of the Class A stock to the detriment of the holders of common stock. Since there are now only 75,000 Class A shares but 426,000 common shares (A. 3), the rulings will give the holders of less than 5% (25,000) of the total shares

(501,000) an ill defined but wide veto power over future changes in the corporation's affairs.

Two main provisions of the declaratory decree forbid what Indiana statutes expressly permit.

First, in forbidding staggered terms for directors, the declaratory decree is directly contrary to an Indiana statute. Section 55-208 of the statute (App. 53a) says that the board of directors may classify the directors and provide for staggered terms. This may be done without amending the certificate of incorporation or bylaws*. The declaratory decree is supportable only if, as contended by the respondents and held by the Illinois courts, the right of cumulative voting granted to all stockholders in the Indiana certificate of incorporation (A. 143) would be violated by the staggered terms of directors. There is no such holding in Indiana. Even where there are constitutional or statutory provisions for mandatory cumulative voting and the provisions are worded as the certificate of incorporation in this case, the courts have uniformly ruled that staggered terms are not thereby forbidden. *Bohannan* v. *Corporation Commission of Arizona*, 82 Ariz. 299, 313 P. 2d 379 (1957); *Humphrys* v. *The Winous Co.*, 165 Ohio St. 45, 133 N.E. 2d 780 (1956); and *Janney* v. *Philadelphia Transp. Co.*, 387 Pa. 282, 128 A. 2d 76 (1956). The Pennsylvania Supreme Court explained why manda-

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* The section reads: "*Classification of Directors.*—It shall be lawful for the board of directors of any railway company . . . , by lot or otherwise, to so classify the members thereof, that one-fourth (as near as may be) shall terminate their official terms as directors at the first annual election thereafter, and one-fourth at each subsequent election; and after being thus classified, the stock and bondholders shall elect only the number of the board of directors necessary to fill the vacancies created by the expiration of the period of services fixed as aforesaid." (Burns Indiana Stat. Ann., sec. 55-208, App. 53a).

tory cumulative voting does not forbid staggered terms (128 A. 2d at 79-80):

> "The cumulative voting strength of a minority is diluted in certain cases not only by staggering the terms of the directors but also by many other rules, methods, systems, and usages of corporate organization, as, for example, having a small board instead of a large number of directors, having longer terms for directors than merely one year, having vacancies on the board filled by election by the board itself as permitted by many statutes. . . . If staggering the terms of corporate directors is unconstitutional because of its interference to some extent with the most efficient use of the right of cumulative voting, the constitutionality of all these practices would presumably be likewise jeopardized for the same reason."
>
> ". . . All that the Constitution provides is that each stockholder should have the right to concentrate his votes on one or more candidates to be chosen in any given election; that right is undisputed, but as to how many candidates there shall be at the election, whether they must consist of all the directors of the corporation, whether they cannot be classified and their elections staggered,—as to these and many other factors which necessarily enter into each situation the Constitution is wholly silent; to write into it any such limiting or qualifying provisions as contended for by plaintiff would be an extreme exercise of judicial legislation."

There are popular misconceptions about cumulative voting. "Cumulative voting has a superficial appeal as a means of assuring minority interests are 'represented' ". See "Mandatory Cumulative Voting: An Anachronism", by Herbert F. Sturdy, XVI The Business Lawyer, 550, 554 (1961). However, in most states statutes expressly permit the classification of directors with staggered terms. See *Model Business Corporation Act Ann.*, §35, ¶2.02, at pp.

595-596 (1960) listing 36 such states and seven in which staggered terms are authorized by implication. The Indiana legislature must be presumed to have had the public interest in mind in allowing staggered terms. The obvious legislative purpose is

> "that, as in the United States Senate, there will always be a portion of the members who are holdovers and thus have had experience in the management of the corporation. The system is designed to provide continuity of management." *Model Bus. Corp. Act Ann.*, §35, ¶4, at p. 598 (1960).

Since votes can be cumulated for the number of directors to be elected at each annual election for staggered terms, the mere statement of the right of cumulative voting does not imply that staggered terms are forbidden.

Illinois is one of two states in which staggered terms have been held invalid because of the peculiar language used in stating the constitutional requirement of cumulative voting. *Wolfson* v. *Avery*, 6 Ill. 2d 78, 94, 126 N.E. 2d 701 (1955); *State* v. *McCune*, 101 S.E. 2d 834, 838 (W. Va. 1958). In the *Wolfson* case the opinion emphasized that the Illinois constitution described cumulative voting for business corporations as entitling the stockholder to "give one candidate as many votes as the *number of directors* multiplied by the number of his shares" (Art. XI, sec. 3, quoted in App. G, *infra* p. 50a); and staggered terms were to be forbidden since this language required shares to be multiplied by "the total number" of directors and not merely those divided into a class. (6 Ill. 2d at 94) In contrast, In *Westlake Hospital Assn.* v. *Blix*, 13 Ill. 2d 183, 191-192, 148 N.E. 2d 471 (1958), which involved a nonprofit corporation not governed by the constitutional language quoted, cumulative voting rights were held not to forbid staggered terms.

In the present case this Illinois prohibition against staggered terms for directors of business corporations has been read into the federal reorganization plan and the Indiana certificate of incorporation. That this is the sole basis of the Appellate Court's ruling is proved by the statement early in its first opinion (App. 4a):

> "The question is whether the power of minority shareholders to cumulate sufficient votes to elect representatives on the board of directors should be diminished or extinguished in contravention of the provisions of a plan of reorganization, a decree of court, and articles of incorporation. *For that is the natural end result of classified directorships and staggered elections.* See *Wolfson* v. *Avery*, 6 Ill. 2d 78, 81-82, 126 N.E. 2d 701, 704." (Emphasis added)

Here the Appellate Court has held, applying an *Illinois* rule of constitutional law, that the cumulative voting provisions of the *federal* reorganization plan and the *Indiana* certificate of incorporation have forbidden staggered terms. The holding was not a mere interpretation of language. The holding was the erroneous application of a rule of law peculiar to Illinois, namely, that the *"natural end result"* of staggered terms is to *"extinguish"* the right of cumulative voting.

Not until the last paragraph of its second opinion did the Appellate Court (App. 28a) discuss the Indiana statutes. It held them to be wholly irrelevant (*"they did not raise any questions of law or fact"*). There was said to be a conflict between section 55-206 providing that directors "shall hold their office for one (1) year and until others are elected in their places" (App. 52a), and section 55-208, permitting staggered terms of more than one year (App. 53a). There is no conflict: section 55-208 qualifies section 55-206 so that the one year term is extended if annual

elections are retained with staggered terms. Even if there were a conflict, the Appellate Court gives no reason for preferring section 55-206 to section 55-208. The opinion concludes by saying that the statutory provision for staggered terms "is not mandatory and the defendant railroad company is not required to violate its commitments to its Class A stockholders" (A. 29a). Here in its last sentence the Appellate Court reverts to the erroneous adjudication, derived from the Illinois constitutional provision and contrary to the Indiana statute, that mandatory cumulative voting forbids staggered terms.

Second, the declaratory decree is contrary to Indiana law in requiring a ⅔ vote of Class A stockholders to amend the provision of the certificate of incorporation that the railroad shall have 13 directors (A. 145). Article IX of the certificate makes it amendable in the manner prescribed by statute (A. 150). A special provision in section 55-207 of the Indiana statute permits the stockholders by majority vote at any annual meeting to determine that the directors shall consist of any number not less than 5 nor more than 13 (App. 52a). This section is not mentioned in the opinions of the Illinois courts.

A ⅔ vote of the Class A stock would be required only if the ⅔ vote clause of the Indiana certificate of incorporation (A. 143) applied to a change in the number of directors. The clause clearly does not apply, since it is limited to amendments concerning

> "the designation, rights, preferences, qualifications, limitations, restrictions, voting rights, values and interests of the Class A stock".

The clause is near the end of a long article, Article IV (A. 135-145 at 143), which has many provisions concerning the rights of Class A stockholders, including cumula-

tive dividends ahead of the common stock, rights on dissolution or liquidation, etc. An introductory sentence in the article sets forth the scope of the matters covered, stating that the Class A stock

> "shall have the following designations, relative rights, preferences, qualifications and limitations, restrictions, voting rights, values and interests." (A. 135)

These words are in the same order and are substantially identical with the description of the scope of the ⅔ vote clause at the end of the article (A. 143). The ⅔ vote clause was drafted so that its scope would coincide with the special rights of the Class A stock described in Article IV. Otherwise it would be difficult to determine what was covered.

Here again the Illinois courts have misconceived the effect of the requirement of cumulative voting. The Appellate Court extends the ⅔ vote requirement as if the number of directors was a part of the right of cumulative voting. Nothing is said in Article IV about the number of directors, which is not a special interest of the Class A stock. The ⅔ vote clause does not apply to it. The Indiana statute, which clearly authorizes a majority vote of the stockholders to change the number of directors, is effectively nullified by the Illinois courts in construing the ⅔ vote clause of the Indiana certificate of incorporation.

For two federal reasons, the Illinois courts were required to apply these disregarded Indiana statutes.

1. The state of incorporation of the new reorganized company was recognized by the reorganization plan as providing the controlling law for the future operations of the railroad. Paragraph B of the plan authorized the transfer of the debtor's property to a "new corporation

. . . formed for this purpose under the corporate laws of such State or States as shall be necessary in order to put into effect and carry out the plan" (App. 34a). The District Court accordingly approved the certificate of incorporation and bylaws of a new Indiana corporation on June 22, 1940 (A. 51-2). Five days later the certificate was issued by the Indiana Secretary of State (A. 152-3). Thereafter the railroad's affairs were required to be governed by Indiana statutes and the Indiana law of corporations. See *In re Ambassador Hotel Corp.*, 124 F. 2d 435, 436-7 (C.A. 2, 1942), *North American Car Corporation* v. *Peerless W. & V. Machine Co.*, 143 F. 2d 938, 940 (C.A. 2, 1944). When the federal District Court here selected an Indiana corporation "as an instrumentality of reorganization", the bankruptcy court "sent it out into the state as fully subject to state law as though the court had had nothing to do with its creation" (124 F. 2d at 437). Once the case was closed as the Bankruptcy Act required and the business started off "on a new and to-be-hoped-for more successful career", the District Court "cast off as quickly as possible all leading strings" which may "throw doubt upon its responsibility" (143 F.2d at 940).

In the present case, more than 20 years after the railroad's incorporation in Indiana as provided by the Bankruptcy Court, the Illinois courts have resorted for guidance to the executed reorganization plan under Illinois law rather than to Indiana statutes. The first Appellate Court opinion completely disregarded Indiana law, for the word "Indiana" was used only twice in the whole opinion; and then in merely stating that the railroad was incorporated and had an office and business in Indiana (App. 1a). But it repeatedly spoke of the rights given the Class A stockholders by the reorganization plan

(App. 1a, 7a, 9a, 10a). The trial court's opinion, while saying that the plan did not govern the operations of the Indiana corporation, stated that the certificate of incorporation "interpreted and construed in the light of the plan of reorganization" fixed the number of directors at 13 and provided for "non-staggered one-year terms" (App. 14a). To the same effect was the second Appellate Court opinion which referred to Indiana statutes in the last paragraph, but rejected their application in favor of the railroad's "commitments to its Class A stockholders". Here the opinion relied on the right of cumulative voting in the federal reorganization plan and the Indiana certificate of incorporation which the court held to include a prohibition of staggered terms as under Illinois constitutional law (App. 29a).

The reorganization plan was not used by the Appellate Court merely to construe the certificate of incorporation as the appellate and trial courts contended (App. 11a, 14a). The plan was used as a source of the decisive rule of law. The plan contained the same brief clause for stating the right of cumulative voting of each of the two classes of stock, "This stock shall have the right of cumulative voting in the election of directors" (App. 44a-45a). The Appellate Court's holding that these simple clauses of the plan forbad staggered terms was a determination of a rule of law, although the notion for it came from peculiar language of the Illinois Constitution (App. 50a) held in Illinois to forbid staggered terms for business corporations. The cumulative voting clause in the certificate of incorporation (A. 143) was much more detailed than the clauses in the plan. The Appellate Court did not construe this language of the certificate, but held that it had the same effect as the clauses of the reorganization plan. The plan was not used to find the meaning of doubtful language in

the certificate. The plan was used to find a rule of law, which was then read into the certificate.

In the guise of construing the certificate, the Appellate Court used the plan to make law. And that law was federal.

The misapplications of the reorganization plan and so of the federal Bankruptcy Act were determinative of the holdings in the declaratory decree as shown by the opinions. From one standpoint the decree gives unwarranted effect to the provision in section 77(f) of the Bankruptcy Act that the corporation organized to carry out the plan "shall put into effect and carry out the plan and the orders of the judge relative thereto" [11 U.S.C. 205(f)]. Further, this statutory admonition is violated when the decree fails to obey the direction in Paragraph B of the plan to follow Indiana law. The decree therefore raises a substantial federal question under a federal statute. The decree seriously affects the relative rights of the common and Class A shareholders of the petitioner railroad. In addition, the Appellate Court's opinions have a far reaching effect as precedent because they encourage resort to old reorganization plans in asserting legal rights properly governed by current state statutes.

2. The Illinois courts' disregard of controlling Indiana statutes is in violation of the Full Faith and Credit Clause of the United States Constitution (Art. IV, sec. 1, App. 50a). It is settled that a state statute is a "public act" within the meaning of the clause. *Carroll* v. *Lanza*, 349 U.S. 408, 411 (1955). The constitutional violation is the fact that the declaratory decree forbids what Indiana law permits this Indiana corporation to do. It is essential that the internal affairs of a corporation be

controlled by the law of one state, the state of incorporation. Here Illinois law has been wrongly applied and Indiana law rejected.

The Appellate Court judges even criticize petitioners for continuing to resist this declaratory relief (App. 25a, 29a-30a). They have not appreciated the heavy overbalance given in the decree to the interests of the Class A stockholders to the detriment of the common stockholders. This suit, properly dismissed as moot by the trial court in March 1960, has been protracted through the years only by the misapplication of Illinois law and the federal Bankruptcy Act in violation of the Full Faith and Credit Clause.

The Illinois courts have reached out in this case to impose a declaratory, summary decree on an Indiana corporation in furtherance of an Illinois rule of constitutional law (no staggered terms for directors of business corporations). This Court has criticized such a use of summary procedure as likely to be "treacherous" and has urged caution against "the subtle tendency to decide public issues free from the safeguards of critical scrutiny of the facts, through use of a declaratory summary judgment". *Eccles* v. *Peoples Bank,* 333 U.S. 426, 434 (1948).

The Illinois Appellate Court, in holding that the case called for a declaratory decree, emphasized "the wide general interest in the stability of preferred stock" and in the petitioner railroad's 75,000 Class A shares (App. 4a, 26a). The declaration harms the holders of the railroad's 426,000 shares of common stock and common shareholders generally to the same extent that it benefits Class A shares. The Illinois Supreme Court has denied review. Since the de-

claratory decree was clearly wrong under federal law, the public interest requires that the decree be reviewed and reversed by this Court.

Conclusion

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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